MINUTES OF BUDGET AND CONTROL BOARD MEETING

JUNE 14 1972

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The Budget and Control Board met in the Governor's Office at 10:00 a. m. on Wednesday, June 14, 1972 with the following Board members in attendance:

Governor John C. West
Senator Edgar A. Brown
Mr. R. J. Aycock
Mr. Henry Mills
Mr. Grady L. Patterson, Jr.

The meeting was also attended by Messrs. P. C. Smith and W. T. Putnam.

The following business was transacted.

PERSONNEL DIVISION - INSURANCE PLAN - Dr. Ronald C. Horn and Mr. Fred B. Haskell appeared before the Board to discuss the present status of the pending insurance program for employees of the State. Mr. Haskell reported that Blue Cross - Blue Shield had agreed to the contract changes which had been requested by the Board in its meeting of May 31, 1972, and indicated that the State was ready to complete its contract upon receipt of final instructions of the Budget and Control Board.

Dr. Horn called the Board's attention to a Source of Funds Statement which he had distributed and asked Mr. P. C. Smith as to the amount of funds which would probably be forthcoming from sources other than those listed.

Mr. Smith stated that, in addition to the funds totaling $6,250,000 as shown on Dr. Horn's statement, between one million and one and one-half million dollars could be expected from other sources. (A copy of Dr. Horn's statement has been retained and is identified as Exhibit I.)

Dr. Horn presented a complete report and recommendations concerning the group insurance plan in which he outlined five elements which he had classified as being essential and five additional proposals which he classified as optional and of lower priority. Of these ten proposals the Budget and Control Board gave tentative approval to eight and modified a ninth. The elements having tentative approval are listed below:

1) The basic plus major medical group health insurance plan initially proposed by South Carolina Blue Cross - Blue Shield and subsequently modified, for all active State employees eligible.

2) The group long-term disability insurance plan initially proposed by Pilot Life and subsequently modified, for all active State employees under age 65.

3) The group term life insurance (plus A. D. & D. benefits) plan, of $2,000 per active employee, proposed by Pilot Life.

4) An adequate budget for the State Personnel Division to assume the State's portion of the role in administering the program.

5) The "employer" should pay the full cost of employee coverage, if at all possible, and the employee himself should pay for any dependents coverage elected (and, where applicable, the extra cost of high option coverage).

6) Pay $4.30 per month per retired employee toward the cost of "supplemental medicare" coverage (add about $154,800 for the first year).

7) Establish a contingency reserve of $100,000 to be held by the State to cover additional employees, etc.

8) Allocate $150,000 to assist in a pilot H. M. O. project for a sample of State employees.

9) Allocate up to $525,000 for a structured program of providing periodic physical examinations for active employees.

A copy of the report and recommendations of Dr. Horn has been retained and is identified as Exhibit II.

It was also agreed by the Board that a public announcement concerning the insurance program should be made as soon as possible, and Governor West requested that Dr. Horn meet with the Public Relations staff of his Office to work out the details of the press release. In addition to the foregoing items, the following were presented:

1) The possible addition of school districts during the fall months.

2) The possible addition of the State Ports Authority and the Public Service Authority.

3) The possible addition of the personnel of the South Carolina State Employees' Association.

However, Governor West and other Board members had pressing appointments and time did not permit the resolving of any of these matters.

PERSONNEL DIVISION - SALARY INCREASES - Mr. Haskell brought up the problem of salary increases but was advised that time did not permit a discussion of this item. He was requested to refer specific questions to Mr. P. C. Smith, State Auditor, for consideration.

SOUTH CAROLINA RETIREMENT SYSTEM - In its meeting of May 2, 1972, the Budget and Control Board approved a Resolution modifying retirement benefits for State employees. In an informal meeting on May 17, 1972 in the Office of Governor West, the Board passed a substitute Resolution.

In the current meeting, the members of the Board confirmed their action of May 17, 1972.

A copy of the amended Resolution has been retained and is designated as Exhibit III.

The meeting adjourned at 11:00 a. m.

EXHIBIT I
JUNE 14, 1972

STATE OF S.C. GROUP INSURANCE PROGRAM

Revised Estimates of First-Year Costs and Available Funds (6/10/72):

*Revised estimated first-year costs

Health Insurance for Active Employees	$4,452,000.
Life, A.D.&D. for Active Employees	411,600.
Administrative Budget for Personnel Division	200,000.
L.T.D. insurance benefits (up to $300 per month) Active Employees	1,421,202.
Total	$6,484,802.

**Estimated "Fair Shares" of Total Funds Needed

State Appropriation	$4,800,000.
Highway Department	1,300,000.
Employment Security Commission	150,000.
Sub-total	$6,250,000.
Other sources and agency shares +	
Total	$

Notes:

*The only cost estimate revised from my earlier June 3rd report concerns the L.T.D. insurance. The $1.4 million figure above reflects adjustments due to: (a) the Board's decision to pay for L.T.D. insurance only up to a maximum benefit of $300 per month (which is equivalent to paying the full cost for those who make up to $6,000 per year); (b) a negotiated rate reduction from the former $.85 to the new $.78 per $100 of "insured payroll" per month; and, (c) my recommendation that the Employer now pay a maximum of $3.90 per month per employee making over $6,000 per year. Thus, the total cost is reduced by about $578,000 compared to my 6/3/72 estimates.

** "Fair Share" estimates are based upon detailed calculations, to be explained to the Board as necessary and desired.

Ronald C. Horn

EXHIBIT II
JUNE 14, 1972

PERSONAL & CONFIDENTIAL

June 3, 1972

Memo to: F.E. Ellis; Director of the Personnel Division, State of South Carolina

From: Professor Ronald C. Horn

In Re: Report and Recommendations Concerning a Group Insurance Program for State Employees

Dear Earl:

The attached report represents my most painstaking effort to refine the cost estimates and otherwise bring the group insurance program decisions to a prompt and successful conclusion. My own recommendations are summarized in section III of the report.

I would like to stress the importance of obtaining decisions on the long-term disability insurance as soon as possible. Generally, we need to know (a) whether the L.T.D. insurance has at least the "conditional" approval of the Board and (b) the exact portion of the L.T.D. cost which is to be paid for by the employer (hopefully, 100%). Until we get these decisions, it will be impossible to finalize rates, guarantees and other important contract provisions with Pilot Life, as we have done with Blue Cross-Blue Shield. Any delays in getting these decisions are going to pose formidable problems in effecting the joint enrollment procedures which we all agree are a "must". Indeed, without first obtaining the Board's decisions on the above, further negotiations with the Pilot - of any kind - would be meaningless and possibly futile.

Both this cover letter and the attached report are for you, your staff and members of the Budget and Control Board. I hope any one of you will feel free to contact me if you have any questions.

Sincerely,

Ron

Ronald C. Horn

PERSONAL & CONFIDENTIAL

REPORT AND RECOMMENDATIONS CONCERNING A GROUP INSURANCE PROGRAM FOR STATE EMPLOYEES

by

Professor Ronald C. Horn
(June 3, 1972)

TABLE OF CONTENTS:

I. ESTIMATED MAXIMUM AMOUNTS NEEDED DURING FIRST YEAR TO FUND ALL PREFERRED BENEFITS FOR STATE EMPLOYEES

ITEM	EMPLOYER FUNDS REQUIRED for FIRST YEAR (ESTIMATED MAXIMUMS)
1. Employer pays full cost of active employees' health insurance for "low option" or "regular" coverage. - - - - - - - - - - - - - - - -	$4,452,000.
2. Employer pays full cost for retirees of health insurance coverage supplemental to Medicare. - - -	298,800.
3. Employer pays full cost of group term life and A.D.&D. insurance with life benefits of $2,000 per active employee under age 65. - - - - - - - - - - - - - -	411,600.
4. Employer pays full cost of group long-term disability insurance for active employees under age 65. - - -	1,999,200.
5. Administrative expense budget for State Personnel Division. -	200,000.
6. Rate fluctuation and contingency reserves. - - - - -	672,000.
7. Allocation for "H.M.O." pilot project. - - - - - - - -	150,000.
8. Allocation for employee physical exam program. - - -	525,000.
Estimated Maximum Total First-Year Funds	$8,708,600.

State Appropriation - - -	-$4,800,000	
Highway Department - - -	- 1,200,000	
Sub-Total	$6,000,000	- 6,000,000.
Estimated maximum amount of "Federal Monies" or other resources needed to fund preferred program conservatively.		$2,708,600.

(See next page for major assumptions and explanations)

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Major Assumptions and Explanations for Illustration I, Page one

Item #1: Blue Cross-Blue Shield guaranteed monthly unit rate for employee's regular coverage is $10.60. The most recent census data suggest that a total of 33,775 State employees would be eligible for the health insurance coverage to be provided active employees. Allowing a margin for error and converting the monthly rates to an annual premium, the calculation would be (35,000 x $10.60 x 12 = $4,452,000).

Item #2: Mr. Gressette estimated that there are currently 3,000 retired State employees, and Blue Cross-Blue Shield now charges $8.30 per month for supplemental coverage for "Medicare" eligibles. (Thus, 3,000 x $8.30 x 12 = $298,800). Active employees over age 65 are to be handled as outlined in the attached summary of our agreement with Blue Cross-Shield.

Item #3: The Pilot Life guaranteed monthly unit rate for active employees' life insurance, including Accidental Death & Dismemberment Benefits, is $.49 per $1,000 of coverage. (Therefore, 35,000 x .49 x 2 x 12 = $411,600). Coverage amounts reduce by 50% at age 65, and terminate upon actual retirement.

Item #4: The Pilot Life guaranteed monthly unit rate on long-term disability insurance (for employees under age 65 only) is $.85 per $100 of "insured payroll", which does not apply to salary amounts in excess of $1,666.67 per month. Estimating the premium, however, is complicated by the fact that a payroll increase is expected at the very time the insurance plan is to become effective. I have assumed a maximum 5.5% average pay increase because of current wage-price ceilings. (Thus, $18,598,000 of estimated monthly "insured payroll" x 1.055 x $.85 per $100 of insured payroll x 12 = $1,999,200). The $.85 rate may change slightly if the employer does not elect to pay 100% of the cost for those who enroll.

Item #5: The State Personnel Division will certainly have additional administrative expenses pursuant to the new employee benefit plans, especially during the first year of operation. A $200,000 allowance should be sufficient for such expenses.

Item #6: Though we were fortunate to secure rate guarantees for the first year (and on a year-to-year basis thereafter), it is simply not possible to forecast accurately the magnitude of potential rate increases which might be effective for the second plan year. The task is particularly complicated by the fact that (a) the Pay Board may soon lift the current restrictions on charges of hospitals and other medical care providers and (b) the Blue Cross-Shield coverages are largely of a service nature (rather than flat dollar hospital per diems, etc.). Some kind of rate increase, at the end of the initial guarantee period, seems virtually inevitable. And total premiums are likely to increase slightly as the State hires additional employees, even if the rates stayed constant.

The "contingency" portion of the reserve amount shown was provided by assuming about 1,200 more active employees than are reflected in the most recent census data. This allows a small margin for both estimating errors and premiums of additional employees hired during the fiscal year July 1, 1972 to July 1, 1973. For employees hired thereafter, it would seem more appropriate to provide the needed funds in the budget for the corresponding fiscal year.

The "rate fluctuation" portion of the reserve amount shown was estimated as follows: on a roughly comparable health insurance plan, Blue Cross-Shield increased the employee monthly unit premium $1.60, $.95 and $.62, respectively, during each of the most recent plan years. Conservatively, the calculation would be 35,000 x $1.60 x 12 = $672,000. From the State's point of view, it could be argued that the rate and contingency reserve should be minimal i.e. perhaps each year should "stand on its own", for budgetary purposes. In fact, the Budget and Control Board might simply say that $10.60 per month per employee is the maximum the Employer will pay for health insurance coverage - and then hold only a small reserve for unanticipated errors and the addition of more State employees during the year. This might cause a problem, though, if rates are increased sharply for the second plan year. If the Board retained the $10.60 dollar figure as a maximum employer contribution, the employee would have to bear the full impact of a rate increase for employee coverage (and also any increase in the rate for dependent coverage). If the Board wanted to "absorb" the rate increase for employee coverage, the absences of a rate fluctuation reserve might require sharp increases in the needed health insurance budget for fiscal 1973-74. For example, a $1 increase in the employee unit rate would require an additional $420,000 per year (35,000 x $1 x 12). A $2 monthly increase would amount to some $840,000 per year.

Item #7: The 150,000 allocated to a pilot H.M.O. project was the amount suggested tentatively by the Budget and Control Board. Mr. Sullivan, President of Blue Cross, has been asked to write the Governor a report on how such an expenditure might best be utilized.

Item #8: The amount shown for an employees' physical examination program was calculated by assuming an average of $15 per year per employee ($15 x 35,000 = $525,000). Further suggestions concerning the proposed program are discussed in a later section.

Miscellaneous: It is important to remember that under group insurance actual premiums are calculated by applying the guaranteed rate to the number of employees who actually enroll. The initial costs to the State could be lower than estimated above, for this reason alone.

II. POSSIBLE APPROACHES TO REDUCE ESTIMATED FIRST-YEAR STATE "OUTLAY"

Approaches	Estimated First-Year "Savings" to State
1. Reduce or eliminate amounts to fund employee physical examination program - - - - - - - - - - - -	(-$175,000 to -$525,000)
2. Reduce or eliminate amounts to fund pilot "H.M.O." project -	(-$50,000 to -$150,000)
3. Reduce employer contribution for retirees' supplemental Medicare coverage to a maximum of $5.30 per month per retiree - - - - - - - - - - - - (Employer contribution limit of $4.30 monthly would save $144,000)	(-$108,000)
4. Reduce insurance administrative budget of State Personnel Division - - - - - - - - - - - - - - - -	(-$80,000)
5. Reduce or eliminate rate-fluctuation and contingency reserves - - - - - - - - - - - - - - - -	(-$336,000 to -$672,000)
*6. Make allowance for anticipated interest earnings on total annual employer funds allocated to the plans - - - - - - - - - - - - - - -	(-$429,000)
**7. Reduce employer contributions toward group long-term disability insurance so as to pay the full cost <u>up to a maximum of $4.25 per month per employee</u>. -	(-$513,000)
8. Use less conservative statistical <u>assumptions</u> concerning the program variables - - - - - - - - -	(Not recommended)
Maximum <u>Possible</u> Reduction In First-Year State Outlay From Above Approaches	$2,513,000

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Amount Needed To Fund All Preferred Benefits During First Year (from illustration I, page one)	$8,708,600
Less General State and Highway Dept. Appropriations	- 6,000,000
Difference	$2,708,600
Potential Savings From Above Program Modifications	- 2,513,000
Possible "deficit"	195,600
Less" Federal Monies" Available This Year	- ?
Margin For Preserving Preferred Benefits	$?

Notes:

*Assumes $6.0 million available at plan inception. Thus, $5.5 million invested for one month, $5.0 million invested two months - - and so on. (Insurance premiums are paid monthly in advance). At 0.3% per month, the annual yield would be about $429,000.

** See the author for explanation of how $4.25 per month was derived.

III. Recommendations of Professor Ronald C. Horn: A Brief Summary

(The following recommendations are based upon information made available to me as of June 3, 1972. They also would be subject to a determination of compliance with wage-price freeze guidelines and approval by the Pay Board and/or other appropriate authorities).

THE ESSENTIAL ELEMENTS

Having carefully studied the appropriate considerations during the past nine months, I am personally and professionally convinced that a group insurance program for our State employees should be established, at this time, with the following five essential elements:

1. The basic plus major medical group health insurance plan initially proposed by S.C. Blue Cross-Blue Shield and subsequently modified, for all active State employees eligible; $4,452,000

2. The group long-term disability insurance plan initially proposed by Pilot Life and subsequently modified, for all active State employees under age 65; 1,421,202

3. The group term life insurance (plus A.D.&D. benefits) plan, of $2,000 per active employee, proposed by Pilot Life; 411,600

4. An adequate budget for the State Personnel Division to assume the State's portion of the role in administering the program; and, 200,000

5. The "employer" should pay the full cost of employee coverage, if at all possible, and the employee himself should pay for any dependents coverage elected (and, where applicable, the extra cost of high option coverage).

These five essential elements would require an estimated maximum employer outlay of about $7,062,800 for the first full year of the program. While this is $1,062,800 more than what we expect from State appropriations and Highway Department sources, it is hoped that federal monies would be available to make up the entire "excess" needed. If not, it seems likely that enough federal monies would be available to provide a significant portion of the necessary funds. And, as noted earlier, interest earnings on appropriated amounts certainly would be large enough to offset any excess needed - at least effectively - by about $500,000. If necessary, the administrative budget for the Personnel Division could be cut by $80,000. If it is absolutely impossible to make up the projected "deficit" from any or all of the above sources, I do not recommend any changes in either the group health or group life insurance plans proposed. Instead, I would reluctantly suggest a reduction in the employer contribution toward the cost of group long-term disability insurance so as to pay the full cost up to a maximum of $4.25 per month per employee (an estimated "savings" of $513,000 for the first year).

LOWER PRIORITY ELEMENTS

I am convinced that the above five elements are so essential that they should be funded in full before any additional features are added to the program. But I am optimistic enough to believe that enough money can be found to (a) fund the five essential elements fully and (b) still leave an ample margin for incorporating one or more additional and desirable program elements. If so, I recommend that the desirable but not absolutely essential features be added in the following order or priority:

6. Pay $4.30 per month per retired employee toward the cost of "supplemental medicare" coverage (add about $154,800 for first year).

7. Establish a rate-fluctuation and contingency reserve to be held by the State (add from $200,000 to a preferable $700,000 for the first year).

8. Allocate $150,000 to assist in a pilot H.M.O. project for a sample of State employees.

9. Allocate up to $525,000 for a structured program of providing periodic physical examinations for active employees (see additional comments below)

10. Pay the rest of the total first-year monthly premium for retirees' supplemental medicare coverage (add $144,000 for first year).

To get a concise picture which should facilitate the decision-making process once the total available moneys are known more precisely, let's take a brief look at the cummulative total costs of my recommendations:

Recommendations	Cummulative Total Employer Dollars Required
First Five Essential Elements (with compromise financing on L.T.D.)	$6,549,800
Add extra cost of preferred L.T.D. financing arrangement	$7,062,800
Add recommendation #6	$7,217,600
Add largest reserve of recommendation #7	$7,917,600
Add recommendation #8	$8,067,600
Add recommendation #9	$8,592,600
Add recommendation #10	$8,736,600

Actually, I believe the employee physical examination program is a high priority item. But a good program cannot be implemented by July 1, 1972. President Sullivan of Blue Cross has some excellent ideas for designing the program, and he has indicated his willingness to do so if he is given at least several more months time. He would design the program so as to prescribe certain diagnostic

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services for various classes of employees (e.g. females between ages x and y would get cancer tests, some employees would be examined only every two years, male employees over age z might have an electrocardiogram - that sort of thing). And Blue Cross would contract with health care providers to deliver the services for agreed upon fees. Indeed, this would be an excellent step toward eventual development of the HMO concept in South Carolina!

My own personal actuarial inclinations would summon me to give high priority to rate and contingency reserves. But I recognize that the decision to establish one in this case is largely a matter of budget philosophy, better left to the Board.

There are many reasons for ranking health coverage on retirees in the lower priority category, among which is that the State is already paying relatively large sums for "Medicare". In contrast, the active employees have no State-financed health plan at the present time. Retirees have no conceptual need for disability income insurance or group term life insurance per se (the latter would be prohibitive in cost, while the former is not available in the marketplace, in any event).

A GENERAL RECOMMENDATION

I rather strongly believe (a) that the State Retirement System ought to be under the Personnel Division (e.g. as a "department" of the latter) and (b) that now would be an excellent time to move swiftly toward this very desirable objective.

The administrative aspects of all employee benefit plans, including retirement plans, are unquestionably a personnel "function". And the Personnel Division heads are best equipped to participate and play a large role in the policy aspects. Group life, health, and disability insurance plans are inexorably related to retirement plan provisions. They need to be coordinated and, in the past, they

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have not been coordinated for State employees. Moreover, we truly need one simple booklet describing all benefits for State employees, insured or otherwise. I will resist the temptation to write a lengthy treatise on the subject at this time, but I still feel the idea itself is worthy of prompt and serious consideration. Indeed, the separateness of the Retirement System entity is going to pose formidable administrative problems as we implement the group insurance plans. I will elaborate if requested to do so by the Budget and Control Board.

IV. ANALYSIS OF REVISED BLUE CROSS-BLUE SHIELD MONTHLY UNIT RATES FOR FIRST PLAN YEAR

Monthly Unit Costs:	Regular Benefits	"High Option"
Employee (active)	$10.60	$11.32
Spouse (not employed by State)	11.90	12.82
Child or Children	5.50	6.46
Combined Totals	$28.00	$30.60

Monthly Cost to Employer: $10.60 per month per covered active employee (recommended maximum)

Dependent Coverage Monthly Costs:

The Employer should pay $10.60 per employee for health insurance; regardless of the option an employee selects.

Thus, the monthly deductions for dependent health coverage effectively would be as follows:

	Regular	High Option*
Spouse only	$11.90	$12.82 + .72 = $13.54
Child or children only	$ 5.50	$ 6.46 + .72 = $ 7.18
Spouse and (child or children)	$17.40	$19.28 + .72 = $20.00
Range	($5.50 to $17.40)	($7.18 to $20.00

*The additional $.72 in each case is the additional monthly amount every employee would be required to pay for employee coverage if he elects the high option alternative ($11.32 - $10.60 paid by the Employer = $.72)

Summary of Monthly Costs to EMPLOYEES:

There will be some employees who will not elect dependent coverage i.e. they will cover only themselves as employees. Moreover, there are some instances where both spouses are "full-time" State employees under the master contract definition. The employees' effective outlay per month would therefore be as follows:

	Employees' Effective Outlay Per Month	
Coverage Provided For	Regular Benefits	High Option Benefits
Employee Only	0	$ .72
Employee and Spouse Only (Both State Employees)	0	$ 1.44
Employee and Spouse only	$11.90	$13.54
Employee and (child or children) only	$ 5.50	$ 7.18 * (+.72)
Employee, Spouse and (child or children)	$17.40	$20.00 * (+.72)

*Additional $.72 on high option is for the case where both employee and spouse are State employees, they elect high option benefits and they cover their child or children. Blue Cross may waive this $.72 for simplicity and equity, if we ask them.

Range of Effective Cost to an Employee Per Month for Health Insurance:

Regular Benefits ($0 to $17.40)
High Option Benefits($.72 to $20.72)

Retirees

State would pay maximum of $8.30 per month per retired State employee

Retired employee would pay $0 (or some portion of cost)

Coverage is special supplement to Medicare and underwritten by Blue Cross-Shield

We are not yet certain whether this rate is guaranteed for first year.

Active Employees Over Age 65

Employee unit rates are same as for all other active employees.

However, coverage "coordinates" with Medicare, for those who have it and/or where it is applicable to a given illness situation. Thus, Blue Cross-Shield has agreed to apply an appropriate "return" portion of the premium to the State - as an identifiable item in the experience rating and retention calculations.

V. NOTES ON PILOT LIFE GROUP L.T.D. AND TERM LIFE INSURANCE PLANS

Group Term Life Insurance

Provides $2,000 group term life insurance plus A.D. & D. benefits for each full-time employee under age 65. Coverage amounts reduce by 50% for active employees age 65 or over. Benefits terminate at retirement.

Dependents may be covered for group term life insurance in the amounts permitted by the S.C. law ($1,000 on spouse and graded downward on children, depending upon their ages. Monthly unit costs are as follows:

Employee Life	$.43 per $1,000	($.86 per month)
Employee A.D.&D.	.06 per $1,000	($.12 per month)
Dependent Life	.45 per "dependent unit" per month	

As recommended earlier, the Employer would pay the entire cost of employee coverage or $.98 per month per active employee; the employee himself would pay for any dependent coverage elected. Dividends are likely on the life insurance. They would be used to reduce employer contributions.

Group Long-Term Disability (L.T.D.)

All full-time employees under age 65 would be provided monthly disability benefits of up to 60% times their basic salary (subject to maximum benefit of $1,000 per month). Benefits begin on the 91st day of total disability and they are payable to age 65 for both accident and sickness disabilities. Benefits are "integrated" at the 60% level with Social Security and certain other group-type plans. The initial monthly unit rate quoted is $.85 per $100 of "insured payroll" (which does not include salary amounts over $1,666.67 per month or payroll for persons over age 65). Dependent coverage per se is not applicable to L.T.D. insurance.

Miscellaneous

We are still in the process of reaching final agreement with Pilot Life on rate guarantees, master contract provisions and other important terms.

EXHIBIT III

JUNE 14, 1972

SOUTH CAROLINA RETIREMENT SYSTEM

RESOLVED, that the State Budget and Control Board, acting in accordance with Section 61-68 of the Act governing the operation of the South Carolina Retirement System, hereby modifies the resolution adopted on May 2, 1972, in the event of the passage of legislation providing for the payment of certain supplemental benefits from the Retirement System, authorizing the actuary to redetermine the accrued liability rate so as to accomplish the liquidation of the unfunded accrued liability over a period of not more than 40 years.

The State Budget and Control Board of the South Carolina Retirement System passed on the preceding resolution on May 17, 1972.

State Budget and Control Board
South Carolina Retirement System

By ____________________
Chairman

ATTEST:

____
Secretary

SOUTH CAROLINA RETIREMENT SYSTEM

RESOLVED, that the State Budget and Control Board, acting in accordance with Section 61-68 of the Act governing the operation of the South Carolina Retirement System, hereby modifies the resolution adopted on May 2, 1972, in the event of the passage of legislation providing for the payment of certain supplemental benefits from the Retirement System, authorizing the actuary to redetermine the accrued liability rate so as to accomplish the liquidation of the unfunded accrued liability over a period of not more than 40 years.

The State Budget and Control Board of the South Carolina Retirement System passed on the preceding resolution on ______________________.

State Budget and Control Board
South Carolina Retirement System

By______________________________
Chairman

ATTEST:

____
Secretary

(6/4)

Putnam

RECEIVED
JUN 5 1972
S. C. STATE
PERSONNEL DIVISION

Earl:

I wanted to enclose this report in a durable and attractive folder of some sort. But I decided to send it to you "as is" so it will be easier to make photo copies for Fred, George and each member of the Budget + Control Board.

You may not agree with some of my recommendations. However, I designed the report contents and format in such a way that I hope they will greatly simplify the remaining decisions to be made.

At this point, I will be "on call" and available to meet with the Board +/or you upon short notice. I think I can be of most help to you, now, by concentrating on finalizing the master contract details. But I am "stopped cold in my tracks" with the Pilot Life unless and until we get decisions on the L.T.D. plan (see my cover letter).

Since 4/19/72, I have ~~spent~~ recorded 49 additional "consulting hours", for your information, and I do hope you feel I am earning my keep.

Ron

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PERSONAL & CONFIDENTIAL

June 3, 1972

Memo to: F.E. Ellis; Director of the Personnel Division, State of South Carolina

From: Professor Ronald C. Horn

In Re: Report and Recommendations Concerning a Group Insurance Program for State Employees

Dear Earl:

The attached report represents my most painstaking effort to refine the cost estimates and otherwise bring the group insurance program decisions to a prompt and successful conclusion. My own recommendations are summarized in section III of the report.

I would like to stress the importance of obtaining decisions on the long-term disability insurance as soon as possible. Generally, we need to know (a) whether the L.T.D. insurance has at least the "conditional" approval of the Board and (b) the exact portion of the L.T.D. cost which is to be paid for by the employer (hopefully, 100%). Until we get these decisions, it will be impossible to finalize rates, guarantees and other important contract provisions with Pilot Life, as we have done with Blue Cross-Blue Shield. Any delays in getting these decisions are going to pose formidable problems in effecting the joint enrollment procedures which we all agree are a "must". Indeed, without first obtaining the Board's decisions on the above, further negotiations with the Pilot - of any kind - would be meaningless and possibly futile.

Both this cover letter and the attached report are for you, your staff and members of the Budget and Control Board. I hope any one of you will feel free to contact me if you have any questions.

Sincerely,

Ron

Ronald C. Horn

PERSONAL & CONFIDENTIAL

REPORT AND RECOMMENDATIONS CONCERNING A GROUP INSURANCE PROGRAM FOR STATE EMPLOYEES

by

Professor Ronald C. Horn
(June 3, 1972)

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I. ESTIMATED MAXIMUM AMOUNTS NEEDED DURING FIRST YEAR TO FUND ALL PREFERRED BENEFITS FOR STATE EMPLOYEES

ITEM	EMPLOYER FUNDS REQUIRED for FIRST YEAR (ESTIMATED MAXIMUMS)
1. Employer pays full cost of active employees' health insurance for "low option" or "regular" coverage. - - - - - - - - - - - - - - - -	$4,452,000.
2. Employer pays full cost for retirees of health insurance coverage supplemental to Medicare. - - -	298,800.
3. Employer pays full cost of group term life and A.D.&D. insurance with life benefits of $2,000 per active employee under age 65. - - - - - - - - - - - - - - -	411,600.
4. Employer pays full cost of group long-term disability insurance for active employees under age 65. - - -	1,999,200.
5. Administrative expense budget for State Personnel Division. -	200,000.
6. Rate fluctuation and contingency reserves. - - - - -	672,000.
7. Allocation for "H.M.O." pilot project. - - - - - - -	150,000.
8. Allocation for employee physical exam program. - - -	525,000.
Estimated Maximum Total First-Year Funds	$8,708,600.

State Appropriation - - -	-$4,800,000	
Highway Department - - -	- 1,200,000	
Sub-Total	$6,000,000	- 6,000,000.
Estimated maximum amount of "Federal Monies" or other resources needed to fund preferred program conservatively.		$2,708,600.

(See next page for major assumptions and explanations)

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Major Assumptions and Explanations for Illustration I, Page one

Item #1: Blue Cross-Blue Shield guaranteed monthly unit rate for employee's regular coverage is $10.60. The most recent census data suggest that a total of 33,775 State employees would be eligible for the health insurance coverage to be provided active employees. Allowing a margin for error and converting the monthly rates to an annual premium, the calculation would be (35,000 x $10.60 x 12 = $4,452,000).

Item #2: Mr. Gressette estimated that there are currently 3,000 retired State employees, and Blue Cross-Blue Shield now charges $8.30 per month for supplemental coverage for "Medicare" eligibles. (Thus, 3,000 x $8.30 x 12 = $298,800). Active employees over age 65 are to be handled as outlined in the attached summary of our agreement with Blue Cross-Shield.

Item #3: The Pilot Life guaranteed monthly unit rate for active employees' life insurance, including Accidental Death & Dismemberment Benefits, is $.49 per $1,000 of coverage. (Therefore, 35,000 x .49 x 2 x 12 = $411,600). Coverage amounts reduce by 50% at age 65, and terminate upon actual retirement.

Item #4: The Pilot Life guaranteed monthly unit rate on long-term disability insurance (for employees under age 65 only) is $.85 per $100 of "insured payroll", which does not apply to salary amounts in excess of $1,666.67 per month. Estimating the premium, however, is complicated by the fact that a payroll increase is expected at the very time the insurance plan is to become effective. I have assumed a maximum 5.5% average pay increase because of current wage-price ceilings. (Thus, $18,598,000 of estimated monthly "insured payroll" x 1.055 x $.85 per $100 of insured payroll x 12 = $1,999,200). The $.85 rate may change slightly if the employer does not elect to pay 100% of the cost for those who enroll.

Item #5: The State Personnel Division will certainly have additional administrative expenses pursuant to the new employee benefit plans, especially during the first year of operation. A $200,000 allowance should be sufficient for such expenses.

Item #6: Though we were fortunate to secure rate guarantees for the first year (and on a year-to-year basis thereafter), it is simply not possible to forecast accurately the magnitude of potential rate increases which might be effective for the second plan year. The task is particularly complicated by the fact that (a) the Pay Board may soon lift the current restrictions on charges of hospitals and other medical care providers and (b) the Blue Cross-Shield coverages are largely of a service nature (rather than flat dollar hospital per diems, etc.). Some kind of rate increase, at the end of the initial guarantee period, seems virtually inevitable. And total premiums are likely to increase slightly as the State hires additional employees, even if the rates stayed constant.

The "contingency" portion of the reserve amount shown was provided by assuming about 1,200 more active employees than are reflected in the most recent census data. This allows a small margin for both estimating errors and premiums of additional employees hired during the fiscal year July 1, 1972 to July 1, 1973. For employees hired thereafter, it would seem more appropriate to provide the needed funds in the budget for the corresponding fiscal year.

The "rate fluctuation" portion of the reserve amount shown was estimated as follows: on a roughly comparable health insurance plan, Blue Cross-Shield increased the employee monthly unit premium $1.60, $.95 and $.62, respectively, during each of the most recent plan years. Conservatively, the calculation would be 35,000 x $1.60 x 12 = $672,000. From the State's point of view, it could be argued that the rate and contingency reserve should be minimal i.e. perhaps each year should "stand on its own", for budgetary purposes. In fact, the Budget and Control Board might simply say that $10.60 per month per employee is the maximum the Employer will pay for health insurance coverage - and then hold only a small reserve for unanticipated errors and the addition of more State employees during the year. This might cause a problem, though, if rates are increased sharply for the second plan year. If the Board retained the $10.60 dollar figure as a maximum employer contribution, the employee would have to bear the full impact of a rate increase for employee coverage (and also any increase in the rate for dependent coverage). If the Board wanted to "absorb" the rate increase for employee coverage, the absences of a rate fluctuation reserve might require sharp increases in the needed health insurance budget for fiscal 1973-74. For example, a $1 increase in the employee unit rate would require an additional $420,000 per year (35,000 x $1 x 12). A $2 monthly increase would amount to some $840,000 per year.

Item #7: The 150,000 allocated to a pilot H.M.O. project was the amount suggested tentatively by the Budget and Control Board. Mr. Sullivan, President of Blue Cross, has been asked to write the Governor a report on how such an expenditure might best be utilized.

Item #8: The amount shown for an employees' physical examination program was calculated by assuming an average of $15 per year per employee ($15 x 35,000 = $525,000). Further suggestions concerning the proposed program are discussed in a later section.

Miscellaneous: It is important to remember that under group insurance actual premiums are calculated by applying the guaranteed rate to the number of employees who actually enroll. The initial costs to the State could be lower than estimated above, for this reason alone.

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II. POSSIBLE APPROACHES TO REDUCE ESTIMATED FIRST-YEAR STATE "OUTLAY"

Approaches	Estimated First-Year "Savings" to State
1. Reduce or eliminate amounts to fund employee physical examination program - - - - - - - - - - - -	(-$175,000 to -$525,000)
2. Reduce or eliminate amounts to fund pilot "H.M.O." project -	(-$50,000 to -$150,000)
3. Reduce employer contribution for retirees' supplemental Medicare coverage to a maximum of $5.30 per month per retiree - - - - - - - - - - - - (Employer contribution limit of $4.30 monthly would save $144,000)	(-$108,000)
4. Reduce insurance administrative budget of State Personnel Division - - - - - - - - - - - - - - - - -	(-$80,000)
5. Reduce or eliminate rate-fluctuation and contingency reserves - - - - - - - - - - - - - - -	(-$336,000 to -$672,000)
*6. Make allowance for anticipated interest earnings on total annual employer funds allocated to the plans - - - - - - - - - - - - - - -	(-$429,000)
**7. Reduce employer contributions toward group long-term disability insurance so as to pay the full cost up to a maximum of $4.25 per month per employee. - - - - - - - - - - - - - - - - - - -	(-$513,000)
8. Use less conservative statistical assumptions concerning the program variables - - - - - - - - -	(Not recommended)
Maximum Possible Reduction In First-Year State Outlay From Above Approaches	$2,513,000

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Amount Needed To Fund All Preferred Benefits During First Year (from illustration I, page one)	$8,708,600
Less General State and Highway Dept. Appropriations	- 6,000,000
Difference	$2,708,600
Potential Savings From Above Program Modifications	- 2,513,000
Possible "deficit"	195,600
Less" Federal Monies" Available This Year	- ?
Margin For Preserving Preferred Benefits	$?

Notes:

*Assumes $6.0 million available at plan inception. Thus, $5.5 million invested for one month, $5.0 million invested two months - - and so on. (Insurance premiums are paid monthly in advance). At 0.3% per month, the annual yield would be about $429,000.

** See the author for explanation of how $4.25 per month was derived.

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III. Recommendations of Professor Ronald C. Horn: A Brief Summary

(The following recommendations are based upon information made available to me as of June 3, 1972. They also would be subject to a determination of compliance with wage-price freeze guidelines and approval by the Pay Board and/or other appropriate authorities).

THE ESSENTIAL ELEMENTS

Having carefully studied the appropriate considerations during the past nine months, I am personally and professionally convinced that a group insurance program for our State employees should be established, at this time, with the following five essential elements:

1. The basic plus major medical group health insurance plan initially proposed by S.C. Blue Cross-Blue Shield and subsequently modified, for all active State employees eligible;

2. The group long-term disability insurance plan initially proposed by Pilot Life and subsequently modified, for all active State employees under age 65;

3. The group term life insurance (plus A.D.&D. benefits) plan, of $2,000 per active employee, proposed by Pilot Life;

4. An adequate budget for the State Personnel Division to assume the State's portion of the role in administering the program; and,

5. The "employer" should pay the full cost of employee coverage, if at all possible, and the employee himself should pay for any dependents coverage elected (and, where applicable, the extra cost of high option coverage).

These five essential elements would require an estimated maximum employer outlay of about $7,062,800 for the first full year of the program. While this is $1,062,800 more than what we expect from State appropriations and Highway Department sources, it is hoped that federal monies would be available to make up the entire "excess" needed. If not, it seems likely that enough federal monies would be available to provide a significant portion of the necessary funds. And, as noted earlier, interest earnings on appropriated amounts certainly would be large enough to offset any excess needed - at least effectively - by about $500,000. If necessary, the administrative budget for the Personnel Division could be cut by $80,000. If it is absolutely impossible to make up the projected "deficit" from any or all of the above sources, I do not recommend any changes in either the group health or group life insurance plans proposed. Instead, I would reluctantly suggest a reduction in the employer contribution toward the cost of group long-term disability insurance so as to pay the full cost up to a maximum of $4.25 per month per employee (an estimated "savings" of $513,000 for the first year).

LOWER PRIORITY ELEMENTS

I am convinced that the above five elements are so essential that they should be funded in full before any additional features are added to the program. But I am optimistic enough to believe that enough money can be found to (a) fund the five essential elements fully and (b) still leave an ample margin for incorporating one or more additional and desirable program elements. If so, I recommend that the desirable but not absolutely essential features be added in the following order or priority:

6. Pay $4.30 per month per retired employee toward the cost of "supplemental medicare" coverage (add about $154,800 for first year).

7. Establish a rate-fluctuation and contingency reserve to be held by the State (add from $200,000 to a preferable $700,000 for the first year).

8. Allocate $150,000 to assist in a pilot H.M.O. project for a sample of State employees.

9. Allocate up to $525,000 for a structured program of providing periodic physical examinations for active employees (see additional comments below)

10. Pay the rest of the total first-year monthly premium for retirees' supplemental medicare coverage (add $144,000 for first year).

To get a concise picture which should facilitate the decision-making process once the total available moneys are known more precisely, let's take a brief look at the cummulative total costs of my recommendations:

Recommendations	Cummulative Total Employer Dollars Required
First Five Essential Elements (with compromise financing on L.T.D.)	$6,549,800
Add extra cost of preferred L.T.D. financing arrangement	$7,062,800
Add recommendation #6	$7,217,600
Add largest reserve of recommendation #7	$7,917,600
Add recommendation #8	$8,067,600
Add recommendation #9	$8,592,600
Add recommendation #10	$8,736,600

Actually, I believe the employee physical examination program is a high priority item. But a good program cannot be implemented by July 1, 1972. President Sullivan of Blue Cross has some excellent ideas for designing the program, and he has indicated his willingness to do so if he is given at least several more months time. He would design the program so as to prescribe certain diagnostic services for various classes of employees (e.g. females between ages x and y would get cancer tests, some employees would be examined only every two years, male employees over age z might have an electrocardiogram - that sort of thing). And Blue Cross would contract with health care providers to deliver the services for agreed upon fees. Indeed, this would be an excellent step toward eventual development of the HMO concept in South Carolina!

My own personal actuarial inclinations would summon me to give high priority to rate and contingency reserves. But I recognize that the decision to establish one in this case is largely a matter of budget philosophy, better left to the Board.

There are many reasons for ranking health coverage on retirees in the lower priority category, among which is that the State is already paying relatively large sums for "Medicare". In contrast, the active employees have no State-financed health plan at the present time. Retirees have no conceptual need for disability income insurance or group term life insurance per se (the latter would be prohibitive in cost, while the former is not available in the marketplace, in any event).

A GENERAL RECOMMENDATION

I rather strongly believe (a) that the State Retirement System ought to be under the Personnel Division (e.g. as a "department" of the latter) and (b) that now would be an excellent time to move swiftly toward this very desirable objective.

The administrative aspects of all employee benefit plans, including retirement plans, are unquestionably a personnel "function". And the Personnel Division heads are best equipped to participate and play a large role in the policy aspects. Group life, health, and disability insurance plans are inexorably related to retirement plan provisions. They need to be coordinated and, in the past, they have not been coordinated for State employees. Moreover, we truly need one simple booklet describing all benefits for State employees, insured or otherwise. I will resist the temptation to write a lengthy treatise on the subject at this time, but I still feel the idea itself is worthy of prompt and serious consideration. Indeed, the separateness of the Retirement System entity is going to pose formidable administrative problems as we implement the group insurance plans. I will elaborate if requested to do so by the Budget and Control Board.

IV. ANALYSIS OF REVISED BLUE CROSS-BLUE SHIELD MONTHLY UNIT RATES FOR FIRST PLAN YEAR

Monthly Unit Costs:	Regular Benefits	"High Option"
Employee (active)	$10.60	$11.32
Spouse (not employed by State)	11.90	12.82
Child or Children	5.50	6.46
Combined Totals	$28.00	$30.60

Monthly Cost to Employer: $10.60 per month per covered active employee (recommended maximum)

Dependent Coverage Monthly Costs:

The Employer should pay $10.60 per employee for health insurance; regardless of the option an employee selects.

Thus, the monthly deductions for dependent health coverage effectively would be as follows:

	Regular	High Option*
Spouse only	$11.90	$12.82 + .72 = $13.54
Child or children only	$ 5.50	$ 6.46 + .72 = $ 7.18
Spouse and (child or children)	$17.40	$19.28 + .72 = $20.00
Range	($5.50 to $17.40)	($7.18 to $20.00

*The additional $.72 in each case is the additional monthly amount every employee would be required to pay for employee coverage if he elects the high option alternative ($11.32 - $10.60 paid by the Employer = $.72)

Summary of Monthly Costs to EMPLOYEES:

There will be some employees who will not elect dependent coverage i.e. they will cover only themselves as employees. Moreover, there are some instances where both spouses are "full-time" State employees under the master contract definition. The employees' effective outlay per month would therefore be as follows:

	Employees' Effective Outlay Per Month	
Coverage Provided For	Regular Benefits	High Option Benefits
Employee Only	0	$ .72
Employee and Spouse Only (Both State Employees)	0	$ 1.44
Employee and Spouse only	$11.90	$13.54
Employee and (child or children) only	$ 5.50	$ 7.18 * (+.72)
Employee, Spouse and (child or children)	$17.40	$20.00 * (+.72)

*Additional $.72 on high option is for the case where both employee and spouse are State employees, they elect high option benefits and they cover their child or children. Blue Cross may waive this $.72 for simplicity and equity, if we ask them.

Range of Effective Cost to an Employee Per Month for Health Insurance:

Regular Benefits ($0 to $17.40)
High Option Benefits($.72 to $20.72)

Retirees

State would pay maximum of $8.30 per month per retired State employee

Retired employee would pay $0 (or some portion of cost)

Coverage is special supplement to Medicare and underwritten by Blue Cross-Shield

We are not yet certain whether this rate is guaranteed for first year.

Active Employees Over Age 65

Employee unit rates are same as for all other active employees.

However, coverage "coordinates" with Medicare, for those who have it and/or where it is applicable to a given illness situation. Thus, Blue Cross-Shield has agreed to apply an appropriate "return" portion of the premium to the State - as an identifiable item in the experience rating and retention calculations.

V. NOTES ON PILOT LIFE GROUP L.T.D. AND TERM LIFE INSURANCE PLANS

Group Term Life Insurance

Provides $2,000 group term life insurance plus A.D. & D. benefits for each full-time employee under age 65. Coverage amounts reduce by 50% for active employees age 65 or over. Benefits terminate at retirement.

Dependents may be covered for group term life insurance in the amounts permitted by the S.C. law ($1,000 on spouse and graded downward on children, depending upon their ages. Monthly unit costs are as follows:

Employee Life	$.43 per $1,000	($.86 per month)
Employee A.D.&D.	.06 per $1,000	($.12 per month)
Dependent Life	.45 per "dependent unit" per month	

As recommended earlier, the Employer would pay the entire cost of employee coverage or $.98 per month per active employee; the employee himself would pay for any dependent coverage elected. Dividends are likely on the life insurance. They would be used to reduce employer contributions.

Group Long-Term Disability (L.T.D.)

All full-time employees under age 65 would be provided monthly disability benefits of up to 60% times their basic salary (subject to maximum benefit of $1,000 per month). Benefits begin on the 91st day of total disability and they are payable to age 65 for both accident and sickness disabilities. Benefits are "integrated" at the 60% level with Social Security and certain other group-type plans. The initial monthly unit rate quoted is $.85 per $100 of "insured payroll" (which does not include salary amounts over $1,666.67 per month or payroll for persons over age 65). Dependent coverage per se is not applicable to L.T.D. insurance.

Miscellaneous

We are still in the process of reaching final agreement with Pilot Life on rate guarantees, master contract provisions and other important terms.

E N D